Filed 7/31/02 Berghoff v. Gavrity CA2/1

NOT TO BE PUBLISHED

IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

SECOND APPELLATE DISTRICT

DIVISION ONE

HERBERT J. BERGHOFF et al., Plaintiffs and Appellants, v. DONALD J. GAVRITY et al., Defendants and Respondents.	B151513 (Super. Ct. No. LC 46027)

APPEAL from an order of the Superior Court of Los Angeles County. Richard B. Wolfe, Judge. Dismissed in part and affirmed in part. Remanded with directions.

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Steiner & Libo and Leonard Steiner for Plaintiffs and Appellants.

Barger & Wolen, Robert J. McKennon, Michael J. Rothman and Vivial I. Orlando for Defendants and Respondents.

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This appeal arises from the trial court's ruling sustaining without leave to amend the demurrer of defendants The Paul Revere Life Insurance Company and Paul Revere Insurance Group (Revere) and Donald J. Gavrity to three of the four causes of action set out in plaintiffs' first amended complaint, seeking policy limit compensatory damages of $649,950 on a disability buy-out insurance policy, on the ground that this lawsuit was barred by the doctrine of res judicata. We order corrections of clerical errors in two trial court minute orders and dismiss the appeal insofar as it challenges the trial court's sustaining without leave to amend Gavrity's demurrer to plaintiffs' claim of negligent misrepresentation against him. We affirm the judgment (order of dismissal) entered following the trial court's sustaining without leave to amend Revere's demurrer to plaintiffs' claims of intentional and negligent misrepresentation against the insurer.

BACKGROUND

In January 1997, Herbert J. Berghoff and Richard M. Rosenthal, as trustee of the Berghoff, Abraham, Friedman & Johnson, Inc. Insurance Trust, filed in superior court a complaint for breach of contract and tortious breach of the implied covenant of good faith and fair dealing against Revere (*Berghoff I*). In the breach of contract cause of action, plaintiffs alleged that when individual disability policies to cover all four BAFJ shareholders were issued in 1992 by Revere to BAFJ (an accounting firm) Berghoff was a shareholder. Plaintiffs also alleged that in April 1994, Berghoff became totally disabled within the meaning of the policy. His claim was filed the same month, and in July, his BAFJ shares were transferred to BAFJ. According to the complaint, pursuant to a shareholder cross-purchase agreement (a prerequisite under the policy to any recovery under the policy), Berghoff was to be paid by BAFJ $92.85 for each share and defendants were obligated to pay the resulting $649,950 on April 29, 1995. The alleged breach was Revere's refusal to pay BAFJ.

In their bad faith cause of action, plaintiffs alleged their motivation for obtaining the insurance coverage was, among other things, to provide security in the event of

plaintiff Berghoff's disability. "Plaintiffs placed trust and confidence in each of the defendants to protect plaintiffs from the adverse consequences of the matters for which they obtained insurance coverage, thus making plaintiffs especially vulnerable to sustaining harm should any of the defendants breach their obligations under the policy." Alleging that ordinary contract damages would not be adequate because such damages would neither require defendant to account fully for "their tortious and improper actions" nor make plaintiffs whole, in addition to compensatory damages, plaintiffs sought punitive damages, prejudgment interest, and costs of suit, including reasonable attorney fees.

Revere removed *Berghoff I* to federal district court, apparently on the basis of diversity jurisdiction.[1] The district court granted Revere's motion for summary judgment. The court concluded the policy was unambiguous, that it obligated Revere to "reimburse" BAFJ for money actually paid by BAFJ to Berghoff, and that because BAFJ had paid no money to Berghoff, the triggering event had not occurred, and Revere was not obligated to make any payment under the policy.[2] The court further ruled that as a matter of law, where no breach of contract occurs, there can be no liability for breach of

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1 We take judicial notice of the records of the federal district court in *Berghoff I* and in the second lawsuit which are included in the parties' joint appendix. (Evid. Code, §§ 452, 459.)

2 That BAFJ had not yet paid Berghoff any money for his interest was undisputed.

The district court's order granting summary judgment sets out the policy language relied on by the parties. Applying California law, the court stated "[t]he overriding goal of contract interpretation is 'to give effect to the parties' mutual intentions as of the time of contracting.' [Citations.] The parties' intent 'is even more important than the strict language used in the contract.' [Citation.] To determine the parties' intent, the court must consider the subject matter of the insurance, the purpose or object the parties had in mind at the time of contracting and the circumstances surrounding the making of the contract. [Citation.]" The court also relied on California law requiring that if a policy's terms are clear, those terms are given the plain meaning a layman would ordinarily attach to them. The court concluded that the controlling, and unambiguous, contract language appeared in "strategic places: the Policy Coverage Page, the Policy Schedule and in the Outline of Coverage," which stated Revere would "'reimburse'" BAFJ for "'monies actually paid'" or "'buy-out expenses actually incurred.'" Further, the court noted, the policy required written proof of the actual buy-out expense amounts and dates incurred, plus the identity of the buyers of the insured's ownership interest. The court held that "both under Insurance Code [section] 10291.5 and [the court's] own construction of the contract, that the Policy language is clear and unambiguous. The court finds that the Policy provides for reimbursement of monies actually paid for the buy-out of Berghoff's interest in BAFJ."

the implied covenant, and granted summary judgment. After the district court denied plaintiffs' motion for reconsideration, the Ninth Circuit Court of Appeals affirmed the summary judgment and denied plaintiffs' petition for rehearing and request for an en banc rehearing.

While their motion for reconsideration was pending in the federal district court, plaintiffs filed the complaint in this action against Revere and Donald J. Gavrity, Jr., a Revere manager in Los Angeles, alleging intentional and negligent misrepresentation by Revere and Gavrity in inducing BAFJ to buy the policies. Plaintiffs alleged Gavrity, "on behalf of himself and all other defendants," represented to plaintiffs that if Berghoff became disabled during the policy period, "defendants" would pay for the expense "incurred" in buying out his shares. Plaintiffs further alleged that defendants knew the representations were false when made and made the representations to induce plaintiffs to act in reliance thereon. Plaintiffs said they were unaware of the falsity of the representations and acted in reliance on them. Plaintiffs alleged they first learned of the falsity of the representations in August 1995 when Revere denied the claim. Plaintiffs alleged compensatory damages of $649,950.

The cause of action for negligent misrepresentation echoed the first cause of action, modified to charge that defendants had no reasonable ground for believing the representations were true when they were made.

Revere filed a removal motion which the federal district court denied on the ground that naming Gavrity defeated diversity jurisdiction, rejecting among other arguments Revere's claim that Gavrity was a sham defendant because under California law an insurance agent cannot be liable for tortious misrepresentation within the scope of his employment. The court wrote, "However, Plaintiffs have alleged both negligent misrepresentation and intentional misrepresentation. The case law in California is well settled that an insurance agent will not be responsible for negligent misrepresentation within the scope of the agent's duties. [Citations.] However, the case law is much less well-settled on the subject of intentional misrepresentation by the agent within the scope

of the agent's duties. No state court has addressed intentional misrepresentation, and the Court notes that the default rule in California is that an agent will be responsible for intentional torts. [Citations.]" Acknowledging it might well occur that the agent cannot be personally liable for his intentional misrepresentation, the court added it was merely noting the issue was unsettled. For that reason, the court was required to "err in favor of remand."

In the superior court, Revere and Gavrity demurred to the complaint on the ground the current action was barred by the doctrine of res judicata. The trial court sustained with leave to amend the demurrer to the negligent misrepresentation claim against Gavrity. The court overruled the demurrer to the intentional misrepresentation claim against Gavrity.[3] The trial court sustained Revere's demurrer to both causes of action with leave to amend.

Plaintiffs first amended complaint added a new paragraph 14: "On January 14, 1997, plaintiffs Berghoff and Rosenthal filed an action in California state court (hereafter 'Berghoff I') for breach of contract, i.e., the Policy, and breach of the concomitant implied covenant of good faith and fair dealing, against defendant Revere and defendant Group. . . . " The first amended complaint also added a plaintiff, Abraham, Friedman & Johnson, Inc., the alleged successor to BAFJ.

In February 2000, Revere and Gavrity filed a demurrer again based on the doctrine of res judicata to three of the four causes of action (excluding the intentional misrepresentation claim against Gavrity). In March, the Honorable Mary Ann Murphy sustained the demurrer without leave to amend on all causes of action "except the second cause of action against defendant Donald Gavrity." According to the June 13, 2001, minute order, the Honorable Richard B. Wolfe ordered dismissal of all but the second

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3 Respondents tell us they intend to appeal from a final judgment, when entered, on the trial court's overruling Gavrity's demurrer to the intentional misrepresentation. In March 2000, Gavrity filed an answer to the first amended complaint. The parties stipulated to a stay of superior court proceedings until final determination of the pending appeal.

cause of action against Gavrity, based on Judge Murphy's order.[4] Berghoff, Rosenthal, and AFJ (collectively "BAFJ") appeal from the June 13, 2001, order of dismissal.

DISCUSSION

I

Before addressing the merits of BAFJ's claim, we first resolve defendants' assertion that the order of dismissal as to Gavrity is not a final judgment for purposes of appeal and should be dismissed. BAFJ's first cause of action for intentional misrepresentation against Gavrity remains pending in the trial court. By stipulation of the parties, the trial court ordered trial court proceedings stayed pending the outcome on appeal. Defendants advise us they believe the trial court erred in overruling Gavrity's demurrer to the intentional misrepresentation and intend to appeal that ruling once a final judgment is entered. Gavrity would, of course, also be entitled to appeal from a disposition adverse to him of the intentional misrepresentation cause of action.

Code of Civil Procedure section 904.1 effectively codifies the common law one final judgment rule -- that an appeal lies only from a final judgment that terminates trial court proceedings by completely disposing of the matter in controversy. (*Griset v. Fair Political Practices Com.* (2001) 25 Cal.4th 688, 697.) The order of dismissal before us does not completely dispose of the matter in controversy. The status of this proceeding also triggers two other policies underlying the general rule. It will generate at least one and perhaps two more appeals. The trial court stay now delays trial court proceedings. (*Kinoshita v. Horio* (1986) 186 Cal.App.3d 959, 967.) Thus, this matter is in the nature of an interlocutory appeal, a context in which the one final judgment rule is strictly applied. (*Id*. at p. 968.) Because the intentional misrepresentation claim remains pending

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4 The parties agree that these minute orders should have excepted the *first* cause of action (intentional misrepresentation), not the second (negligent misrepresentation.). Given this joint representation and the context of this case, we order the clerical error appearing in the March 23, 2000, and June 13, 2001, minute orders corrected nunc pro tunc (see Disposition, *infra*). (See, e.g., *Campbell v. Southern Pacific Co*. (1978) 22 Cal.3d 51, 62-63.)

in the trial court and because Gavrity intends to appeal the trial court's overruling his demurrer, we apply the rule and dismiss that aspect of the appeal.

II

BAFJ claims its tort claims in this lawsuit are not barred by the federal district court's ruling in *Berghoff I*. We conclude otherwise.

"In examining the sufficiency of [a] complaint, '[w]e treat the demurrer as admitting all material facts properly pleaded, but not contentions, deductions or conclusions of fact or law. [Citation.] We also consider matters which may be judicially noticed.' [Citations.] '[W]e give the complaint a reasonable interpretation, reading it as a whole and its parts in their context. [Citation.] When a demurrer is sustained, we determine whether the complaint states facts sufficient to constitute a cause of action. [Citation.] And when it is sustained without leave to amend, we decide whether there is a reasonable possibility that the defect can be cured by amendment: if it can be, the trial court has abused its discretion and we reverse; if not, there has been no abuse of discretion and we affirm. [Citations.] The burden of proving such reasonable possibility is squarely on the plaintiff.' [Citation.]" (*First Nationwide Savings v. Perry* (1992) 11 Cal.App.4th 1657, 1662.)

Invoking the primary right theory, BAFJ says the current lawsuit involves a different primary right than the one involved in *Berghoff I* and is, therefore, not barred by the doctrine. BAFJ says its right not to be subjected to tortious acts is different from its right to damages arising from a breach of contract. However, the cases BAFJ cites to support this proposition did not involve the situation presented here: a first lawsuit for breach of contract *and* a tortious bad faith claim, followed by a second lawsuit grounded exclusively in tort. Revere asserts the final judgment in *Berghoff I* bars this action because this lawsuit involves the same cause of action. Moreover, says Revere, the theories of liability brought in this lawsuit could and should have been brought in *Berghoff I*. We conclude Revere has the better of the argument.

"A valid final judgment on the merits in favor of a defendant serves as a complete bar to further litigation on the same cause of action. [Citations.] . . . California has consistently applied the 'primary rights' theory, under which the invasion of one primary right gives rise to a single cause of action. [Citations.] . . . It is clearly established that '. . . there is but one cause of action for one personal injury [which is incurred] by reason of one wrongful act.' [Citations.]" (*Slater v. Blackwood* (1975) 15 Cal.3d 791, 795.)

"[T]he 'cause of action' is based upon the harm suffered, as opposed to the particular theory asserted by the litigant. [Citation.] Even where there are multiple legal theories upon which recovery might be predicated, one injury gives rise to only one claim for relief. 'Hence a judgment for the defendant is a bar to a subsequent action by the plaintiff based on the same injury to the same right, even though he presents a different *legal ground* for relief.' [Citations.]" (*Id*. at p. 795.)

"The violation of *one primary right* constitutes a single cause of action, though it may entitle the injured party to many forms of relief, and the relief is not to be confounded with the cause of action, one not being determinative of the other." (*Wulfjen v. Dolton* (1944) 24 Cal.2d 891, 895-896.)

However, the phrase "cause of action" is often used indiscriminately to mean the specific counts or legal theories presented as bases for relief for an injury rather than the primary right. (*Slater v. Blackwood*, *supra*, 15 Cal.3d at p. 796.) The first usage is common in pleading, but is not the term's meaning for res judicata analysis. (*Ideal Hardware, Etc. Co. v. Dept. of Emp.* (1952) 114 Cal.App.2d 443, 448.) For purposes of res judicata, cause of action "is the right sought to be established, not the remedy or relief, which determines the nature and substance of the cause of action." (*R & A Vending Services, Inc. v. City of Los Angeles* (1985) 172 Cal.App.3d 1188, 1194.)

Under the rule against splitting a cause of action, a litigant cannot withhold an issue from the first lawsuit and litigate that issue in a second action when it is within the scope of the cause of action alleged in the first lawsuit. (*Kronkright v. Gardner* (1973) 31 Cal.App.3d 214, 217.) "If the matter was within the scope of the action, related to the

subject matter and relevant to the issues, so that it *could* have been raised, the judgment is conclusive on it despite the fact that it was not in fact expressly pleaded or otherwise urged. The reason for this is manifest. A party cannot by negligence or design withhold issues and litigate them in consecutive actions. Hence the rule is that the prior judgment is *res judicata* on matters which were raised or could have been raised, on matters litigated or litigable." (*Sutphin v. Speik* (1940) 15 Cal.2d 195, 202.) "Whatever grievance a litigant may have at the time he is involved in a legal contest must be included in his pleadings then. If he neglects or chooses not to do so the judgment entered will be deemed final as to such question as may have been a potential issue. [Citation.]" (*Seaboard Finance Co. v. Carter* (1951) 106 Cal.App.2d 738, 742.) The doctrine extends to facts and conditions as they existed when the issues in the first action arose and to the legal rights and relations of the parties as set by the facts determined by that judgment. (*Lord v. Garland* (1946) 27 Cal.2d 840, 849.)

BAFJ claims the two lawsuits were critically different because the claim in *Berghoff I* was that Revere failed to fulfill BAFJ's claims under the contract, whereas in the current lawsuit the claim is that BAFJ was misled into buying the contract. However, application of these standards leads us to conclude the trial court did not err in sustaining Revere's demurrer without leave to amend. Plaintiffs' primary right in both lawsuits was the alleged harm caused by BAFJ's not receiving insurance benefits from Revere. That plaintiffs framed the first lawsuit, at least in part, on contract interpretation does not change the fact that the second lawsuit, framed exclusively in tort terms, complained of the same harm. The right plaintiffs sought to enforce in both lawsuits was BAFJ's right to payment by Revere.[5]

In addition, critical facts giving rise to the fraud allegations in this lawsuit (misrepresentations about when payment would be made) necessarily occurred and were

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5 Gavrity's addition as a named defendant in this lawsuit does not change the cause of action for res judicata purposes. In any event, it is undisputed that Gavrity was Revere's agent.

known before BAFJ secured the disability buy-out policy. Nonetheless, the accounting firm chose to pursue only the claim that Revere was required to pay it when the expenses from Berghoff's disability were "incurred," in the sense of obligated to pay, rather than, as the federal district court ruled, when the firm paid and was entitled to reimbursement. Thus, when Revere declined to pay the policy limits requested by BAFJ, the issues raised in both lawsuits could have been raised. BAFJ's failure to raise them gives rise to the bar aspect of the doctrine of res judicata.

Moreover, plaintiffs introduced the possibility of a tort recovery in *Berghoff I* by alleging "tortious . . . actions" by Revere based on its failure to pay. Plaintiffs' allegation in *Berghoff I* that they had placed trust and confidence in Revere to protect the firm from the adverse consequences of Berghoff's disability is tort language at the core of their claims in this lawsuit.

We find no error in the trial court's sustaining without leave to amend Revere's demurrer to the negligent misrepresentation and intentional misrepresentation claims against it.

DISPOSITION

The trial court is directed to correct its March 23, 2000, minute order nunc pro tunc, to read: "Demurrer is sustained, without leave to amend, res judicata, on all causes of action except the first cause of action against defendant Donald Gavrity. Counsel for plaintiff states that he would not change complaint if given another opportunity to amend the complaint. Notice is waived."

The trial court is directed to correct its June 13, 2001, minute order nunc pro tunc, to read: "The demurrer of defendants, Paul Revere Life Insurance Company and Donald J. Gavrity, Jr., to the first amended complaint having been sustained without leave to amend as to all causes of action with the exception of the first cause of action against defendant Gavrity by Judge Mary Anne Murphy presiding in Department Northwest "Z" on 3/23/01, and Judge Murphy having been assigned to the central district of the Superior

Court prior to the assignment of the above-captioned case to this court by the Presiding Judge of this district, the court now makes the following order: Good cause appearing therefor, the above entitled action is hereby dismissed under the provisions of section 581 et sequitur of the Code of Civil Procedure, with prejudice as to each cause of action set forth in the first amended complaint with the exception of the first cause of action as to defendant Donald J. Gavrity."

That part of the appeal challenging the trial court's sustaining without leave to amend defendant Gavrity's demurrer to the claim of negligent misrepresentation against him is dismissed.

In all other respects, the judgment (order of dismissal) is affirmed.

The parties are to bear their own costs.

NOT TO BE PUBLISHED.

ORTEGA, J.

We concur:

SPENCER, P.J.

RICO, J.*

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* Judge of the Los Angeles Superior Court assigned by the Chief Justice pursuant to article VI, section 6 of the California Constitution.